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In the Supreme Court of the United States

OCTOBER TERM, 1937

No. 128

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

JOHN H. THERRELL, ALSO KNOWN AS J. H. THERRELL

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 49–52) is not reported. The opinion of the Circuit Court of Appeals for the Fifth Circuit (R. 61–64) is reported in 88 F. (2d) 869.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered March 9, 1937. (R. 66.) Petition for

certiorari was filed June 9, 1937, and was granted October 11, 1937. (R. 67.) The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether amounts received by the respondent as compensation for services rendered as liquidator of certain Florida State banks and paid entirely out of funds of the banks are immune from Federal taxation on the ground that such a tax would be an unconstitutional burden upon the State.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix A, *infra*, pp. 47–54.

STATEMENT

The essential facts as they appear from the pleadings and as stated in the opinion of the Board of Tax Appeals (R. 49–52) may be summarized as follows:

In July, 1930, the respondent was appointed, by the Comptroller of the State of Florida, liquidator of the Bank of Bay Biscayne, a state banking institution of the State of Florida, located at Miami, Florida (R. 19–20), and duly qualified as such liquidator (R. 20–25).

The respondent thereafter, in the years 1930 and 1931, was appointed liquidator for other banking

institutions within the State of Florida and duly qualified as such. (R. 25–47, 50.) The appointment of liquidators to administer insolvent banking institutions by the Comptroller of the State of Florida is authorized by the laws of Florida. (Florida Laws, 1929, Vol. I, c. 13576, Sec. 19, amending Sec. 4162, Revised General Statutes.) (R. 50.)

The respondent, in assuming his duties as liquidator, received no commission from the government of the State of Florida and took no oath of office. He was appointed by and served entirely at the pleasure of the Comptroller and was required to give bonds in each of his undertakings as liquidator. (R. 50.)

The respondent's duties as liquidator were to handle litigation involving the liquidation of the banks and to dispose of their assets to the best advantage of depositors and others concerned. As liquidator the respondent exercised supervision over a number of persons employed in various capacities to assist in the liquidation of the several banks, and was, himself, under the direct supervision of the Comptroller. During the years 1931 and 1932 the respondent devoted all of his time to his duties as liquidator except on occasions when, as inactive president of a bank at Ocala, Florida, he attended directors' meetings. (R. 50.)

The respondent's compensation for his services in liquidating the several banking institutions was

determined and paid to him by the Comptroller on a commission basis, not in excess of 5% of the amounts collected by him and turned in to the State Treasury, and was paid out of the moneys recovered by him in the liquidation of the various banking institutions. (R. 50, 52.) Sections 4162, 4164, Revised General Statutes, *infra,* pp. 48–52. The respondent's compensation as liquidator of the several banking institutions amounted to $8,555.61 in 1931 and $39,448.07 in 1932. (R. 51.)

The respondent, contending that these amounts were received by him as an employee or officer of the State of Florida, claimed an exemption from Federal income tax. The Commissioner of Internal Revenue held that the compensation was taxable income and determined the deficiencies here in issue in the amounts of $108.78 and $6,329.53, for the years 1931 and 1932, respectively. (R. 49, 52.) The Board of Tax Appeals held (R. 52) that the respondent was neither an officer nor an employee of the State of Florida and that his only relation to that State was a contractual relation by which he was to furnish service and that the imposition of a Federal income tax on his compensation received on a percentage basis out of moneys recovered by him as liquidator of closed banks could not be deemed to be an interference with the governmental functions of the State of Florida, or to place a prohibited burden upon the State of Florida in the exercise of its governmental func-

tions, and determined the deficiencies in respondent's income taxes for the years 1931 and 1932, which are in issue here. (R. 53.)

The Circuit Court of Appeals, one judge dissenting, reversed the decision of the Board of Tax Appeals.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the compensation received by the respondent as liquidator was not subject to Federal income taxation.

2. In failing to hold that the respondent was neither an officer, an employee, nor an agent of the State engaged in an essential governmental function.

3. In failing to hold that, even if the respondent were an officer, an employee, or an agent of the State, taxation of the compensation received by him out of funds of the insolvent banks imposes no prohibited burden upon the State.

SUMMARY OF ARGUMENT

The only question in this case relates to the application of the constitutional principle that a Federal tax upon an individual is invalid if it threatens to destroy the dual system of government. It is unnecessary in this case to question the principle of *Collector* v. *Day,* 11 Wall. 113, since even if that principle be accepted the Com-

missioner's determination may be sustained upon any of three separate grounds.

I

The services of the respondent were not rendered in connection with an essential governmental function. His duties were not those of regulating state banking institutions, but consisted in liquidating certain insolvent banks and trust companies. Florida statutes subject liquidators, just as solvent banks, to supervision by the regular bank examiners. The purpose of the liquidation is not to insure sound banking practices generally, but to benefit the particular individuals who were creditors and stockholders in the closed banks. The liquidator has no regulatory functions and his activities consist only of those which are found in the operation of a solvent bank.

As was the case in *Helvering* v. *Powers,* 293 U. S. 214, the respondent was conducting a private enterprise, was paid out of private assets, and was engaged in an activity essentially different from the regulation of the going concern. In this case, as in that, the controlling principle must be that which forbids the State from withdrawing normal sources of Federal revenues by itself conducting the business.

The fact that 32 states permit the Federal Deposit Insurance Corporation to serve as a liquidator of insolvent state banks seems conclusive that

the function is not one essential to the independence of the states from the central government.

II

The respondent's compensation was paid out of the assets of the insolvent bank, and not out of the State treasury. It seems necessarily to follow that a tax upon this compensation cannot possibly be an unconstitutional interference with the State. Such was the unequivocal decision in *Flint* v. *Stone-Tracy Co.*, 220 U. S. 107, 174. While the lower courts are in conflict, it seems to us to be abundantly plain that a tax upon compensation from private funds is wholly irrelevant to the finances of the State. And if the tax be imposed upon an individual, and if it cannot affect the State treasury, *ex hypothesi*, it is impossible for it to be an interference with the functions of the State. It is to be noted that our argument does not here go to the point of urging the validity of a tax upon officials whose compensation is derived from fees collected for the State; these fees are government revenues, while the assets of an insolvent bank are not.

This Court has often pointed out that the doctrine of tax exemption must be limited to the necessity of protecting our dual system of government. *Helvering* v. *Powers, supra*, pp. 224–225, *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 523. To grant tax exemption to individuals who are not

paid out of public funds would be extending the doctrine far beyond its necessity and would have alarming consequences upon the Federal revenues. See *Willcuts* v. *Bunn*, 282 U. S. 216, 225; *Susquehanna Co.* v. *State Tax Commission* (*No. 1*), 283 U. S. 291, 294.

III

The respondent was neither an officer nor an employee of the state. He took no oath of office and received no commission. The Board found that he was neither an officer nor an employee. The Florida statutes require that the regular bank examiners supervise not only banks but also their liquidators; this is inconsistent with viewing a liquidator himself as another employee of the Comptroller. The respondent was appointed for a particular job. He was paid by the job, in a fluctuating amount which was greater than the Comptroller's salary. He continued his private connections with the private banking business. His qualifications were such that the supervision of the Comptroller was probably nominal. Certainly, in view of the findings of the Board of Tax Appeals, the supervision must be taken to have been consistent with the status of a contractor, rather than that of an employee.

ARGUMENT

This case presents the question whether the Federal Government may constitutionally impose a tax

upon the compensation of the respondent as liquidator of certain insolvent Florida banks and trust companies, paid entirely out of the assets of the liquidating banks and trust companies. In *James* v. *Dravo Contracting Co.*, *Mason* v. *Tax Commission, and Ryan* v. *Washington,* Nos. 3, 7 and 8, this Term, the Government raised the question whether any non-discriminatory tax could be considered a threat to our dual system of government, when applied to a private person whose only claim of immunity rested on the fact that he dealt with the Government. In the oral argument of that case the Government suggested that the application of that principle to officers and employees of the respective governments turns upon the decision of this Court as to the importance to the independence of the state and central governments that their employees be exempt from taxes upon their salaries. In the three cases then under consideration the Government took the position that reexamination of the cases such as *Collector* v. *Day,* 11 Wall. 113, was there unnecessary.

Similarly, we are of the view that the present case is not such that we should ask for a reexamination of the cases which hold or assume that preservation of our dual system of government requires that the employees or officers of the central and state governments be exempted from a nondiscriminatory tax imposed by the other sovereign. This is the case, we submit, because: (1) the liqui-

dation of insolvent banks is not an essential governmental function; (2) the doctrine of a constitutional exemption from taxation because of the immunity of the sovereign can have no application to compensation paid from private funds; and (3) the respondent is not an officer or employee of the State. Any one of these conclusions is sufficient to sustain the Commissioner's determination.

Before discussing these propositions, it should be observed that the question before the Court is solely one of the application of a constitutional principle. The earlier Revenue Acts exempted the "compensation of all officers and employees of a state or any political subdivision thereof." (Sec. II (b), c. 16, 38 Stat. 114; Sec. 4, c. 463, 39 Stat. 756; Sec. 201 (a), c. 63, 40 Stat. 300.) However, since the Revenue Act of 1918 there has been no comparable provision, Congress having left "the constitutional question as to the authority of Congress to tax certain salaries to be settled by the courts * * *." (S. Rep. No. 617, 65th Cong., 3d Sess., Pt. 1, p. 6.) While Sections 22 of the Revenue Acts of 1928 and 1932, here involved, contain no exemption of government salaries, Articles 643 of Treasury Regulations 74 and 77, *infra*, recognize the principle of constitutional immunity and exempt "compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function

* * *." Our argument does not go beyond the Regulation, as we interpret it, but if it should be construed to exempt compensation paid out of private funds, we then submit that it is invalid. The Treasury Department cannot "either limit the provisions of the statute or define the boundaries of their constitutional application." *Helvering* v. *Powers,* 293 U. S. 214, 224.

I

THE SERVICES OF RESPONDENT WERE NOT IN CONNECTION WITH AN ESSENTIAL GOVERNMENTAL FUNCTION

Whether or not respondent is an officer or employee of the State, and even though his compensation were derived from State funds, the payments are subject to federal taxation because his services were not rendered in connection with an essential governmental function.

It is settled that there can be no claim of immunity unless the compensation be given for services performed for the State in connection with activities of a nature such that Federal taxation would violate "the necessary protection of the independence of the national and state governments within their respective spheres." *Helvering* v. *Powers,* 293 U. S. 214, 225; see *South Carolina* v. *United States,* 199 U. S. 437; *Ohio* v. *Helvering,* 292 U. S. 360, 368–369. The question for decision is whether the liquidation of financial institutions

by the states is such an essential governmental function.

The discussion will, we believe, be clarified if the issues be narrowed at the outset. The Government concedes that the *regulation* of the state banking institutions is an essential governmental function. We anticipate that respondents will not argue that the *operation* of state financial institutions is an essential governmental function, or deny that a state-owned bank, and its employees, would be subject to Federal taxation. Such, at any rate, was the decision in *State of North Dakota* v. *Olson,* 33 F. (2d) 848 (C. C. A. 8th), appeal dismissed for want of jurisdiction, 280 U. S. 528, and such are the plain implications of *South Carolina* v. *United States, Ohio* v. *Helvering,* and *Helvering* v. *Powers,* all *supra.* Further, we have no doubt but that the State has an important public interest in the orderly liquidation of its financial institutions; each of the states has made statutory provision for a special method of administrative liquidation of these institutions.[1] In our view of the case, the question is thus reduced to the inquiry as to whether liquidation of financial institutions, admittedly within the "zone of debatable ground" (*Brush* v. *Commissioner,* 300 U. S. 352, 365), is

[1] In Appendix B, *infra*, p. 55, we have made a rough classification of the types of machinery provided for the relief or liquidation of insolvent financial institutions by each of the states.

more akin to the operation or to the regulation of the state financial institutions.[2]

The answer given by the Florida statutes seems relatively clear. Section 4159 of the Revised General Statutes, as amended, *infra,* authorizes the Comptroller to appoint a bank report analyst and examiners to examine into the affairs of banks and their liquidators. Section 4161, *infra,* requires that banks and liquidators be examined at least twice a year.[3] It is improbable that the liquidator would be subject to the State regulatory machinery unless he were viewed as substantially similar to the operating bank.

The expenses of liquidation are paid out of the assets and income of the insolvent institution, rather than by the appropriation of public funds out of the state treasury (see *infra,* pp. 21–35). This seems more akin to the conduct of a particular business enterprise than to state regulation.

The purpose of liquidation is to return to the creditors and shareholders as much of their depos-

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[2] The characterization, in *Relfe* v. *Rundle*, 103 U. S. 222, 225, of the statutory successor of an insurance company was: "He is an officer of the State, and as such represents the State in its sovereignty while performing its public duties connected with the winding up of the affairs of one of its insolvent and dissolved corporations." This was directed toward an entirely different question, his succession to foreign assets, and has no application here.

[3] Apparently, however, an examination fee is not charged the liquidator.

its, loans and investments as possible (see Secs. 4162, 4164, *infra*). The undoubted public interest in securing the largest feasible return, leading in turn to the establishment of expert, administrative liquidation proceedings, does not alter the fact that the activity is being undertaken not to insure sound banking practices generally, but to benefit the individuals who are interested in the affairs of a particular institution. The liquidator's efforts, just as those of the officials of a solvent bank, are directed exclusively toward the benefit of those concerned with the operations of the single bank.

None of the liquidator's activities are regulatory in nature. The actual activities of the liquidator consist chiefly of the sale of assets and the collection of loans, in order to realize cash assets. The activities of a solvent bank include these and, in addition, making loans and investments and receiving deposits. The liquidator, accordingly, does a part of the business of a solvent bank. A reduction in the scope of the activities, without any change in their nature, obviously does not convert a business enterprise into one which is regulatory in character.

If there were doubt, it would seem removed by the decision of this Court in *Helvering* v. *Powers*, 293 U. S. 214. The facts here are strikingly similar to those there considered. Powers was trustee of the Boston Elevated Railway Company. There, as here, the enterprise was one such that its *regulation*

was an essential governmental function. There, as here, the public interest suggested government operation when the affairs of the private enterprise became deranged. It can make no difference that in the *Powers* case the government leased the property for a temporary period while here it took control for the purpose of liquidation; in each case the property was privately owned and the government management was for the benefit of the creditors and shareholders of the enterprise. Indeed, the important and general governmental interest in the maintenance of low fares made operation of the Elevated Railway much more "public" in nature than in the case of the insolvent bank. In the *Powers* case, as here, the property of the enterprise remained subject to state taxation.[4] In the *Powers* case, as here, the enterprise was subject to Federal taxation before it was taken over by the State. Accordingly, we think the decision in the *Powers* case conclusive of the issue here presented. There the Court said (p. 225):

> The principle of immunity thus has inherent limitations. * * * And one of these limitations is that the State cannot withdraw sources of revenue from the federal taxing power by engaging in businesses which constitute a departure from usual governmental functions and to which, by

[4] We assume that the absence of exemption in the Florida statutes means that the property held by the liquidator remains subject to taxation.

> reason of their nature, the federal taxing power would normally extend. The fact that the State has power to undertake such enterprises, and that they are undertaken for what the State conceives to be the public benefit, does not establish immunity. * * *

Finally, the Court in the *Powers* case (p. 227) brushed aside the argument that a temporary operation was more of a governmental function than would be outright ownership and a continuing government operation. That conclusion is equally applicable here.

This Court has already indicated the fallacy which underlies the reasoning of the court below. The majority said (R. 64):

> We are of opinion that the establishment and supervision and orderly winding up of State banks is a true governmental function of the State, resting not only on its fiscal needs and powers but also on its police power.

In other words, from "establishment and supervision" the majority made an effortless leap to the quite different matter of "orderly winding up." This, as we have shown, is more akin to operation than to regulation. And in *Ohio* v. *Helvering*, 292 U. S. 360, 369, this Court said: "the police power is and remains a governmental power, and applied to business activities is the power to regulate those activities, not to engage in carrying them on."

See also *South Carolina* v. *United States*, 199 U. S. 437, 457–458; *United States* v. *California*, 297 U. S. 175.

In both the *South Carolina* and the *Powers* cases the Court has not only considered the effect on Federal revenues, but has apparently made this the basis of its decision as to the asserted governmental character of the activity. In *South Carolina* v. *United States*, *supra*, p. 455, the Court summarized its earlier analysis by saying: "Indeed, if all the States should concur in exercising their powers to the full extent, it would be almost impossible for the Nation to collect any revenues." And in *Helvering* v. *Powers*, *supra*, p. 225, the Court defined a limitation upon the doctrine of intergovernmental tax immunity as the principle that "the State cannot withdraw sources of revenue from the federal taxing power by engaging in businesses which constitute a departure from usual governmental functions and to which, by reason of their nature, the federal taxing power would normally extend." See also *United States* v. *California*, *supra*, p. 184.

Here, the state bank [illegible] its employees were fully subject to Federal taxation while the institution was solvent. They would remain subject to taxation during the period of liquidation had the stockholders voted to liquidate and dissolve. Under the settled doctrine of the *South Carolina* and *Powers* cases, the fact that the State chooses itself to op-

erate or liquidate the institution cannot take this usual source of revenue out of the reach of the Federal Government.

Brush v. *Commissioner*, 300 U. S. 352, has no application to the circumstances of this case. There the activity of supplying water was such that, had it been abandoned, "in a very real sense * * * the city itself would then disappear." The maintenance of a water supply was held to be a "necessary auxiliary" of essential governmental activities. (P. 371.) Such is not the case here. The State of Florida would continue to exist without substantial change whether or not a State official undertook the liquidation of insolvent banks. Indeed, even its regulation of active banks would be substantially unaffected.

Finally, we urge that the liquidation of insolvent banks cannot be an essential governmental activity, such that the maintenance of our dual system of government requires freedom even from taxation of the employees, because many states permit or require the activity to be undertaken by the Federal Government itself. The majority of the states have made provision for the appointment of the Federal Deposit Insurance Corporation as receiver or liquidator of an insolvent state bank the deposits of which are insured with the Corporation. In two States the provision is mandatory.* In twenty-five

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*Louisiana Laws of 1934, Act No. 180, Sec. 4; Mississippi, Banking Code of 1936, Sec. 112.

States (including Florida) the appointment of the Corporation is permissive.[6] In five States the pre-existing statutes[7] have received informal administrative construction to authorize the Corporation to serve as receiver, liquidator or agent of the state officials.

The Federal Deposit Insurance Corporation is a federal instrumentality, the capital stock of which was subscribed by the United States, the Federal Reserve Banks and the members of the Corporation (Sec. 8, c. 89, 48 Stat. 162, 168–169). We are unable to see how the function of liquidating state

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[6] Alabama, Laws of 1935, Act. No. 395, Sec. 3; Arkansas, Laws of 1933, Act No. 15, Sec. 1 (as construed); California, Laws of 1935, ch. 501, Sec. 2; Colorado, Laws of 1937, ch. 100, Sec. 3; Florida, Laws of 1937, Act No. 7, Sec. 1; Idaho, Laws of 1935, ch. 9, Sec. 3; Kansas, Laws of 1937, ch. 76, Sec. 3; Michigan, "New Banking Code" of 1937, S. B. No. 2, Sec. 125; Minnesota, Laws of 1937, ch. 404, Sec. 3; Montana, Laws of 1937, S. B. No. 81, Sec. 3; Nebraska, Banking Code of 1935, ch. 8, Sec. 3; Nevada, Laws of 1935, ch. 87, Sec. 3; New Mexico, Laws of 1935, ch. 16, Sec. 3; North Carolina, Laws of 1935, ch. 81, Sec. 4; North Dakota, Laws of 1935, ch. 95, Sec. 3; Ohio, Banking Code of 1937, Sec. 710–89d; Oklahoma, Laws of 1935, p. 197, Sec. 3; South Carolina, Laws of 1935, Act No. 339, Sec. 3; South Dakota, Laws of 1935, ch. 60, Sec. 1; Tennessee, Laws of 1935 (Ex.), ch. 42, Sec. 2; Texas, Laws of 1935, ch. 183, Sec. 3; Utah, Laws of 1935, ch. 8, Sec. 3; Vermont, Laws of 1935, Act No. 173, Sec. 1; West Virginia, Laws of 1935, ch. 17, Sec. 3; Wisconsin, Laws of 1935, ch. 469, Sec. 220.081, amended by laws of 1937, ch. 284.

[7] Illinois, Jones' Ill. Stats., vol. 3, Sec. 10.11; Kentucky, Carroll's Statutes, Sec. 165a–17; Maine, Revised Statutes, 1930, ch. 57, Sec. 52; Pennsylvania, Purdon's Stats., Tit. 7, Sec. 482; Washington, Remington's Revised Statutes, Sec. 3269.

banks could be extended to a Federal instrumentality by 32 States (including Florida) and yet be an activity which must be exempted from Federal taxation because such a protection is necessary to the independence of the state governments. Compare *Helvering* v. *Powers, supra,* p. 225; *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 575; *Ambrosini* v. *United States,* 187 U. S. 1, 7; *Collector* v. *Day,* 11 Wall. 113, 125, 127. It is evident that at least 32 of the States do not feel that their sovereignty, or their independence in our dual system, is impaired if they allow the Federal Government actually to undertake the liquidation of state banks in place of the State. *A fortiori,* this activity is not an activity so essential to the governmental powers of the State that the Federal Government should be held unable even to tax the compensation of those engaged in performing it.

Any decision to the contrary would present the most perplexing problems. The Federal Deposit Insurance Corporation, we are informed, is actually liquidating, or acting as a receiver for, insolvent state banks in eight States.[8] It would be difficult for the Federal Government to tax the compensation paid those engaged in this activity if this Court were to hold the tax immunity of the activity essential to the independence of the state governments. Yet a decision that the Federal Govern-

[8] North Dakota, South Dakota, Oklahoma, Mississippi, Louisiana, West Virginia, Ohio, and Michigan.

ment could not tax its own employees because this would threaten the independence of the state governments is incomprehensible. In our view, the only solution to this dilemma is the common sense suggestion that, if the states generally delegate the task to the Federal Government, the activity cannot be essential to their independent sovereignty.

II

A TAX ON COMPENSATION PAID FROM PRIVATE FUNDS CONTAINS NO THREAT TO THE DUAL SYSTEM OF GOVERNMENT

1. The respondent's compensation was fixed by the Comptroller of the State, although it was not to exceed five percent of the cash collections. But the Florida statute expressly provides that the respondent's compensation should be "paid out of the assets of such bank, banker, banking firm, banking or trust company, or corporation" (Sec. 4164, Revised General Statutes, as amended, *infra*) of which the respondent was liquidator. The payment of the respondent's compensation was made by the Comptroller out of moneys held by the State Treasurer "as a special deposit for the use and benefit of the creditors" of each particular insolvent bank or trust company for which the respondent was appointed as liquidator (Sec. 4162, Revised General Statutes, as amended, *infra*).

It results that respondent's compensation was not paid out of State funds. It came out of the

income or assets of the insolvent bank. Whether the compensation was large or small in no manner affected the State finances. There is no substantial difference, so far as the interest of the State is concerned, between the compensation paid respondent and that paid the bank president prior to the insolvency. The mechanics of the payment differ, it is true, in that the respondent was paid by an order drawn by the Comptroller on the fund held by the State Treasurer, while the bank president was probably paid by an order on the bank drawn by the cashier. In addition, it is recognized that the Comptroller supervised the liquidator in a somewhat different manner than he did the going concern (see, however, Section 4159 of the Revised General Statutes, *infra*). But these circumstances do not change the obvious fact that in each case the directing official receives his compensation not from the State but from the assets and income of the bank.

2. We have, then, a case in which there can be no contention that the tax here involved would in any manner affect the finances of the State. The respondent bases his whole claim to immunity on the fact that he was appointed by and served under a State official. The question is whether, even assuming respondent to be an officer or employee of the State whose services were in connection with the performance of an essential governmental function, he may claim the protection of the State's

sovereign immunity from Federal taxation when his compensation is taken wholly from private funds.

In our view this Court has unequivocally settled this question. In *Smith* v. *Northern Trust Co.*, argued with *Flint* v. *Stone-Tracy Co.*, 220 U. S. 107, the stockholder's bill alleged that the Trust Company (No. 411, 1910 Term, R. 6) "receives a considerable and valuable income from its frequent appointment by the courts of Illinois as trustee, receiver, assignee, guardian, conservator, executor or administrator". From this it was argued that the Congress was without constitutional power to impose such a tax. This Court rejected the argument, and said (p. 174):

> Nor is the special objection tenable, made in some of the cases, that the corporations act as trustees, guardians, etc., under the authority of the laws or courts of the State. Such trustees are not the agents of the state government in a sense which exempts them from taxation because executing the necessary governmental powers of the State. The trustees receive their compensation from the interests served, and not from the public revenues of the State.

Again, in *Helvering* v. *Powers*, 293 U. S. 214, 223, the Court gave some emphasis to the fact that the taxpayer's compensation was derived from the Elevated Railway rather than from the State.

Notwithstanding the unequivocal declaration of this Court in *Flint* v. *Stone-Tracy Co.*, the rulings

of the lower courts and of the administrative officials are conflicting. The majority of the court below thought, because the payments were controlled by the Comptroller rather than the bank or its creditors, that "it is superficial to say that they pay him." (R. 62). It followed this decision in *Tunnicliffe* v. *Commissioner*, 88 F. (2d) 873, pending in this Court, No. 129. The Circuit Court of Appeals for the Sixth Circuit, in *Bettman* v. *Warwick*, 108 Fed. 46, 48, with respect to a stamp tax on the qualifying bond required of a notary public, said that it was immaterial whether the notary's compensation came from the State or from private persons. In *Freedman* v. *Commissioner*, 92 F. (2d) 150 (C. C. A. 3d), pending on petition for writ of certiorari, No. 597, the court held that an employee of the State Department of Justice, whose salary was paid from the assets of liquidating banks, was immune from taxation. In *Hoskins* v. *Commissioner*, 84 F. (2d) 627 (C. C. A. 5th), the court held the compensation of one employed in a school cafeteria to be exempt, without considering that it was paid out of cafeteria receipts.

On the other hand, the Circuit Court of Appeals for the Second Circuit, in *McLoughlin* v. *Commissioner*, 89 F. (2d) 699, 701, pending in this Court, No. 287, held, with respect to the salary of counsel employed by the State and paid out of the assets of liquidating insurance companies, that "there can be no exemption from Federal taxation where, as

here, taxation would result in no burden upon the governmental power of the state." In *Helvering* v. *Curren,* 90 F. (2d) 621 (C. C. A. 2d), the court, while holding that the compensation of counsel to a county clerk was tax-exempt, said (p. 622):

> A tax does not as such impede state officials in the performance of their duties; it can scarcely be said to invade the state's sovereignty, save as it may require the official's salary to be correspondingly raised. Even that would seem to be generally an "indirect" result, for the rise need not inevitably follow; the incumbent might accept the cut rather than throw up his position. * * *

In *Miller* v. *McCaughn,* 27 F. (2d) 128 (C. C. A. 3d), the court held taxable the compensation of an auditor, appointed by the state court and paid by the surety companies who applied for bond-writing. It said (p. 128):

> The exemption of state employees from federal income tax rests on the ground that the agencies the state employs in government should not be burdened by federal taxes, which would lessen the state's power to employ, and compel it to pay more for the services of its employees. * * *

In *New York Trust Co.* v. *United States,* 63 C. Cls. 100, 102, certiorari denied, 274 U. S. 756, the court held the plaintiff's compensation, received for acting as executor, guardian, a comimttee, etc., in state courts, to be taxable, in part because "its compen-

sation was not paid by the State but indirectly by the private person or persons interested in the estate in each case." In *Saxe* v. *Anderson,* 19 F. Supp. 21, 26 (S. D., N. Y.), certiorari denied, No. 398, this Term, pending on appeal, Judge Knox held the compensation of a referee taxable; cases in other jurisdictions were put aside because the taxpayer before him derived his compensation from the private litigants. This factor was said to be "of importance and goes to the heart of the basis of the exemption, viz., the burden imposed upon the sovereign." In *Harman* v. *Helvering,* 90 F. (2d) 622 (C. C. A. 2d), pending on petition for writ of certiorari, No. 433, this Term, the court held taxable a court stenographer's fees from litigants. It based the decision on the conclusion that the services were not essentially governmental, but said (p. 623):

> it is tempting to say that, as the state's treasury is not concerned, the tax must necessarily be valid * * * no one has ever given any other rational reason for the whole doctrine.*

Finally, in *Commissioner* v. *Ogden,* 62 F. (2d) 334 (C. C. A. 1st), the court held a court auditor, whose compensation was paid by the county, to be tax-

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*The omitted portions of the quotation state (1) "the cases will scarcely bear out such a test," and (2) "we refused to base our decision on it in *McLoughlin* v. *Commissioner,* 89 F. (2d) 699." The first statement, we believe, is due to a failure to consider the distinction advanced below, pp. 31–32, and the second is plainly wrong.

exempt. It said (p. 335) that "non-statutory auditors, generally paid by the parties, stand upon a very different footing."

The Board of Tax Appeals has followed a vacillating course. In *Todd* v. *Commissioner*, 15 B. T. A. 962, and *Cahn* v. *Commissioner*, 13 B. T. A. 1362, it held trustees and executors appointed by state courts taxable on their compensation, which was paid out of private funds. But in *Cochrane* v. *Commissioner*, 26 B. T. A. 1167, and *Winne* v. *Commissioner*, 27 B. T. A. 369, it rejected the test of the source of the compensation and held the fees of masters in chancery to be exempt. Finally, it has held the source of the compensation to be a persuasive, even though not controlling, factor, and has held receivers appointed by state courts to be taxable. *Wright* v. *Commissioner*, 29 B. T. A. 1267; *Abbott* v. *Commissioner*, 30 B. T. A. 227; *Strickland* v. *Commissioner*, 32 B. T. A. 804.

The Bureau of Internal Revenue has not been consistent in its rulings.[10] Prior to 1934 the Commissioner of Internal Revenue held that the source of the taxpayer's compensation was immaterial.[11]

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[10] Since the rulings seek to interpret a constitutional rather than a statutory provision, those prior to 1934 did not gain an added force by virtue of Congressional reenactment. Compare *Helvering* v. *Powers*, 293 U. S. 214, 225.

[11] See O. D. 1053, 5 Cumulative Bulletin 106 (fees of deputy sheriffs); I. T. 1316, I-1 Cumulative Bulletin 105 (compensation of deputy bank examiners appointed by a state bank examiner and paid out of the assets of insolvent banks); I. T. 1652, II-1 Cumulative Bulletin 71 (compensa-

However, since that date, the Commissioner has consistently taken the position that the compensation as an officer or employee of a State or political subdivision is subject to the federal income tax if it is not paid out of public funds, since the imposition of the tax in such a case does not burden the State so as to constitute a substantial and direct interference with the exercise of a sovereign function.[12]

3. It seems quite plain to us that a tax on compensation paid out of private funds, *ex hypothesi*, cannot contain a threat of destruction of our dual system of government.

In *James* v. *Dravo Contracting Co., supra,* and the related cases, the Government argued that cost alone could not be the test of a forbidden interfer-

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tion of state employees paid in part out of Federal contributions to the state); I. T. 1693, II-1 Cumulative Bulletin 72 (fees of public administrators); I. T. 2030, III-1 Cumulative Bulletin 117 (fees of public administrator in Montana); I. T. 2214, IV-2 Cumulative Bulletin 46 (compensation of receiver of insolvent Kansas bank); G. C. M. 60, V-1 Cumulative Bulletin 45 (compensation of secretary of Kansas State Fair Board paid largely from fair earnings); G. C. M. 11625, XII-1 Cumulative Bulletin 69 (fees of special masters in chancery in Illinois); I. T. 2710, XII-2 Cumulative Bulletin 79 (employees of state banking department paid out of insolvent bank assets); I. T. 2677, XII-1 Cumulative Bulletin 141 (compensation of teacher paid out of federal grants).

[12] See G. C. M. 13488, XIII-2 Cumulative Bulletin 156 (bank liquidator); I. T. 2859, XIV-1 Cumulative Bulletin 101 (state Emergency Relief Administrator); G. C. M. 14116, XIV-1 Cumulative Bulletin 102 (public administrator); G. C. M. 14957, XIV-2 Cumulative Bulletin 130 (notary public).

ence with the dual system of government—the cost must be imposed specially on those who dealt with the other sovereign, i. e., a discriminatory tax, or it must be regulatory or prohibitory in effect, before the private person could find shelter behind the cloak of sovereign immunity. But even in the case where the tax on an individual is such that it is held to be a threat to our dual system of government, it is to be noted that it possesses this potential danger only because it will be reflected in the sovereign's treasury. A tax on one who is not the sovereign cannot possibly affect that government unless in some manner the amounts paid by the sovereign will be increased because of the tax. Thus, while no tax on an individual should be considered to contain a threat to the dual system of government merely because it results in an added cost to the sovereign,[13] a tax on an individual cannot even be considered as a possible threat to that dual system unless it does result in added costs to the sovereign. The tax which is imposed on an individual, and is in no manner passed on to the sovereign, is one which is wholly irrelevant to the sovereign. Such, we submit, is the case here.

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[13] We believe the discussion of the constitutional doctrine of inter-governmental tax immunity is clarified if the two senses of the term "burden" be distinguished. It may on the one hand mean an added *cost* to the sovereign. This does not necessarily mean that the tax is unconstitutional. See, e. g., *Trinityfarm Co.* v. *Grosjean*, 291 U. S. 466; *Liggett & Myers Co.* v. *United States*, 299 U. S. 383. The

There is nothing inherently unconstitutional in taxing one who is employed by or who deals with the sovereign. The government official must pay property, inheritance and excise taxes to the other sovereign; his income other than the salary paid by the government is taxable. The only conceivable basis, it seems to us, for exempting his government-paid salary is because a tax so measured might be thought to be an interference with our dual system because it would result in the necessity that a higher salary be paid out of the public treasury.

In this case, even if it be assumed that a net income tax will so discourage the respondent that he will refuse to perform his services without higher pay, the resulting increase in compensation cannot affect the State. The additional compensation will come from the assets and income of the insolvent banks. This may have some tendency to reduce the recovery by creditors and stockholders, just as the taxation of the president of a solvent state bank may have the same effect. But it obviously cannot result in an added charge against the State treasury.

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term "burden" may on the other hand mean an *interference* with the sovereign such as to threaten our dual system of government. A tax with such consequences is invalid. It is, therefore, a serious logical fallacy to reason that an added cost is a "burden," that a "burden" is unconstitutional, and that a tax which results in an added cost is therefore unconstitutional.

The epochal dictum of Chief Justice Marshall, that the power to tax is the power to destroy (*McCulloch* v. *Maryland,* 4 Wheat. 316, 427) was considered by him to be an inexorable constitutional principle because questions of degree were "so unfit for the judicial department" (p. 430). This Court has long since rejected both the premise and the conclusion of this bold syllogism.[14] But even if this great dictum be given its full force, its application leads inevitably to the conclusion that the power to tax the respondent contains the possibility of destruction, not for the State of Florida, but only for the assets of the insolvent bank. And, so far as we know, none has ever suggested any reason why insolvent banks, as opposed to those which are solvent, are essential to the independence of the State from the central government.

It will be noted that our present argument does not go to the point of urging the validity of a tax on all government employees for whose compensation the state is reimbursed by private persons. To illustrate, the clerk of a court or a sheriff may be authorized to collect fees and fines, and may be allowed to retain a certain amount or percentage. We do not believe we should be justified in urging, if these officials collected the money in exercise of

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[14] See, in the body of constitutional doctrine relating to intergovernmental tax immunity, *Plummer* v. *Coler*, 178 U. S. 115; *Greiner* v. *Lewellyn*, 258 U. S. 384; *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 523; *Willcuts* v. *Bunn*, 282 U. S. 216; *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279, 282.

an essential governmental function, that they were paid out of private funds. The state requires the fees and fines in order to swell its revenues and the officials are paid in return for performing an essential governmental function. They are not, as in the present case, paid out of private funds in which the State has no interest. The clerk's fees are government revenues; the assets of an insolvent bank are not.

In summary, our two main propositions seem almost indisputably clear: The reason a government officer or employee is tax exempt on his salary, but in no other respect, must be because it is feared that a tax so measured would impose additional costs on the public treasury, in a manner such as to threaten our dual system of government. If the salary or compensation is in fact paid out of private funds, there cannot possibly be a danger to the public treasury or to the sovereign.

4. This Court has often pointed out that the doctrine of tax exemption must be limited to the necessity of the principle upon which it is founded. "Springing from that necessity it does not extend beyond it". *Board of Trustees* v. *United States*, 289 U. S. 48, 59. Accordingly, if the taxpayer cannot affirmatively show that his subjection to taxation threatens to disrupt our dual system of government, he will not be granted immunity. *Helvering* v. *Powers*, 293 U. S. 214, 224–225; *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 523; *Indian Ter-*

ritory Oil Co. v. *Board,* 288 U. S. 325, 328; *Willcuts* v. *Bunn,* 282 U. S. 216, 225; *Educational Films Corp.* v. *Ward,* 282 U. S. 379, 391; *National Bank* v. *Commonwealth,* 9 Wall. 353, 362.

Correlatively, this Court has been aware of the imperative importance that there be no attrition of the sources of tax revenues. In *Willcuts* v. *Bunn,* 282 U. S. 216, 225, the Court declared:

> The limitation of this principle to its appropriate applications is also important to the successful working of our governmental system. The power to tax is no less essential than the power to borrow money, and, in preserving the latter, it is not necessary to cripple the former by extending the constitutional exemption from taxation to those subjects which fall within the general application of non-discriminatory laws, and where no direct burden is laid upon the governmental instrumentality, and there is only a remote, if any, influence upon the exercise of the functions of government.

See also *Helvering* v. *Powers,* 293 U. S. 214, 225; *United States* v. *California,* 297 U. S. 175, 184–185; *Susquehanna Co.* v. *State Tax Commission (No. 1),* 283 U. S. 291, 294. This factor becomes of increasing significance as the scope and variety of governmental functions expand. It is unnecessary to cite statistics to demonstrate the dependence of the federal government, and of many state governments, upon the revenues obtained from the income tax upon individuals. These revenues are

seriously impaired by *Collector* v. *Day, supra,* and the cases which have followed it. To push the doctrine of employee immunity into new fields, and to grant the largesse of tax exemption even to those who are not paid out of public funds, would have the most alarming consequences. The taxation of such individuals would not contain even a remote or conjectural effect on state operations—indeed, such taxation seems to us demonstrably and inescapably to be wholly irrelevant to the finances of the State. On the other hand, to exempt from taxation this new and very large category[15] of

[15] It is impossible to estimate the number of persons who would gain an exemption from federal taxation if it were held that their employment or designation by State officials resulted in an immunity whether or not they were paid from state funds. The taxpayers who have sought rulings from the Bureau of Internal Revenue (in addition to the published rulings cited in footnote 4, *supra*) since 1934 are illustrative; masters in chancery (G. C. M. 16242); unemployment compensation commission (G. C. M. 18152); teachers in federal land grant colleges (G. C. M. 14622); state board of health, paid with federal funds (G. C. M. 18089); coaches of athletic teams paid with admission receipts (G. C. M. 16169); costs collected by justices of the peace (G. C. M. 15949); members of National Guard paid by the United States (G. C. M. 13188).

In the field of insolvent banks alone, it is to be noted that 47 of the 48 States expressly provide that the expenses and compensation of the liquidator shall be paid out of the assets of the insolvent bank. (The state statutes are listed in Appendix B, *infra*, p. 55. Only Maine has no express provision.)

individuals would have a certain and a serious impact upon government revenues. We respectfully submit that the Constitution cannot require that the federal and state governments be crippled in their search for revenues when the only compensatory gain would be a wholly capricious exemption of individual taxpayers, paid out of private funds, and differing from their fellow business men who are taxed only in that, under a somewhat different form of state supervision, they conduct the business of an insolvent instead of a solvent institution.

III

THE RESPONDENT WAS NOT AN OFFICER OR EMPLOYEE OF THE STATE BUT WAS AN INDEPENDENT CONTRACTOR

Apart from the fact that respondent's compensation came from private rather than State funds, and whether or not the liquidation of banks is an essential governmental function, he cannot claim exemption from taxation because he is not an officer or employee of the State.

It is thoroughly settled that compensation paid by the State, even for services in connection with an essential governmental function, is not immune from federal taxation if the relationship of the taxpayer be that of an independent contractor, rather than that of an officer or employee. *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514; *Lucas* v. *Reed*,

281 U. S. 699; *Lucas* v. *Howard,* 280 U. S. 526; *General Construction Co.* v. *Fisher,* 295 U. S. 715. The only question, then, is one of the factual circumstances of this case. We submit that they require the conclusion that respondent was not an officer or employee of the State.

1. It is unnecessary to elaborate the argument that respondent was not an officer of the State of Florida. His duties were restricted to liquidating the specific banks and trust companies for which he was appointed. He received no commission from the Governor and took no oath of office. The Florida statutes require that each officer receive a commission from the Governor and take an oath of office; neglect or refusal so to qualify results in the office being vacant. Comp. Gen. Laws of Florida, Secs. 460, 461; *Advisory Opinion to the Governor,* 14 Fla. 277; *Advisory Opinion to the Governor,* 65 Fla. 434. The Board found that respondent was not an officer (R. 52) and the majority of the court below, while declaring the respondent to be "a public official and an instrumentality," recognized that he was "not a public officer in the full sense" (R. 64).

2. The more difficult question is whether respondent is an employee or an independent contractor. To a large extent this turns on the particular circumstances of the case. The findings of the Board of Tax Appeals as to the evidentiary

facts are conclusive.[16] To the extent that the ultimate conclusion of the Board is based on these evidentiary facts it cannot be reviewed. *Helvering* v. *Rankin*, 295 U. S. 123, 131; *Elmhurst Cemetery Co.* v. *Commissioner*, 300 U. S. 37. The decision of the Board (R. 52), that the tax was imposed on "one who is neither an officer nor an employee of the government and whose only relation to it is that of contract" may in part be based upon factual evidence, such, for example, as the extent of the control exercised over respondent by the Comptroller. Accordingly, the judgment of the court below must be reversed unless this Court should hold as a matter of law (cf. *Helvering* v. *Tex-Penn Oil Co.*, 300 U. S. 481, 491; *Bogardus* v. *Commissioner*, No. 15, this Term) that *no* factual circumstances could serve to alter a conclusion that respondent was an employee of the State. We submit that this is not the case and that, on the contrary, respondent was plainly not an employee of the State.

The court below held that respondent was "not a public officer in the full sense" (R. 64). It did not hold that respondent was an employee of the

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[16] Respondent assigned error neither to the admission or rejection of evidence nor to the findings of the Board. Accordingly, this record contains no statement of the evidence before the Board (R. 58). See *Helvering* v. *Ward*, 79 F. (2d) 381 (C. C. A. 8th); *Winnett* v. *Helvering*, 68 F. (2d) 614 (C. C. A. 9th); *Commissioner* v. *Proctor Shop*, 82 F. (2d) 792 (C. C. A. 9th); *Cass* v. *Helvering*, 83 F. (2d) 841 (C. C. A. 8th).

State. This would seem to compel the conclusion that respondent was, as the Board held, an independent contractor. Instead, the court created a new and amorphous category, "a public official and an instrumentality appointed by the State," and assigned the privilege of tax exemption to persons who fell within it. This, we submit, was patent error.

The Florida statutes seem persuasive that the liquidator is not an employee of the Comptroller but is, rather, a contractor who after his appointment has substantially the status which the bank, whose affairs he is to conduct, had prior to its insolvency. The same act which provided for the appointment of a liquidator provides in Section 14, amending Section 4159 of the Revised General Statutes (*infra,* p. 47):

> That the Comptroller in the supervision of banks and trust companies, shall have power to employ a bank report analyst and not more than twelve discreet and competent persons to examine into the affairs of every bank, banker, banking company or trust company, doing business in the State, *and liquidators thereof,* except National Banks, and the persons so employed shall have power to make a thorough examination into all the affairs of each and every such bank, banker, banking firm, banking company or trust company *and liquidating agencies,* at any time; and in doing so shall have access to all the books, papers, records, securities and assets of all kinds, and shall be author-

> ized to examine any of the officers, directors, agents or employees, of such bank, banker, banking firm, banking company, trust company *or liquidators thereof,* under oath, and such examiners shall make a full and detailed report to the Comptroller of the conditions of each bank, banking company, trust company *or liquidating agency* thereof so examined. Provided, that no person connected with the banking business, either as an officer, director, agent or employee shall be so employed. [Italics added.]

It is too plain for argument that this statute authorizes the employment of examiners to supervise banks *and their liquidators.*[17] Thus, the Florida

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[17] The Supreme Court of Florida in *Ex parte Amos*, 100 Fla. 687, on habeas corpus released the Comptroller who had been taken into custody because of malfeasance. The original affidavit alleged that the Comptroller willfully employed officers, etc., of the Bank of Bay Biscayne "in connection with the examination of the Bank." The State court held the affidavit consistent with the inference that the Comptroller had merely employed assistants to administer the affairs of the bank after it had ceased to do business. By obvious inadvertence (due to repeating only the first clause of Section 14, which has ambiguous punctuation), the court said (p. 690): "The affidavit does not allege that the petitioner employed persons connected with the banking business as a bank report analyst or as bank examiners *or liquidators.*" (Italics added.) The inference of the italicised words is (1) plainly not necessary to the decision of the case, (2) patently inadvertent, and not that "considered dictum" (*Hawks* v. *Hamill*, 288 U. S. 52, 59) which federal courts will ordinarily follow, and (3) has not been adopted by the State officials, as shown by the record in this case.

statutes treat liquidators as having the status of active banks, even to the point of subjecting them to the same examination by the Comptroller's employees. This is wholly inconsistent with any view that the liquidator himself is an "employee" of the Comptroller.

The other circumstances of this case offer cogent support to this conclusion. The respondent was not hired by the month or year, or for an indefinite period of time. He was appointed, just as would be any contractor, to do a particular job. When he undertook to liquidate other institutions he received a new appointment for each one (R. 50; R. 19–20, 31–32, 33–34, 43–44). Were he an employee, one would suppose that the Comptroller would merely direct him to liquidate the other institutions as well. Instead, the procedure applicable to a contractor who assumes additional contracts was followed.

Similarly, respondent was paid by the job, instead of by the month or year as would be the case with an employee. His compensation was $8,555.61 in 1931, and $39,448.07 in 1932. A 460 per cent increase in compensation over the previous year is assuredly more typical of the contractor than the employee of the State. Especially is this the case when it is noted that even in 1931 his compensation was considerably in excess of that of the Comptroller, his supposed superior, who in 1931 received only $6,000 (Laws of 1931, ch. 15720, sec. 1).

There is nothing in the appointments or the statutes which forbids a liquidator from carrying on a private business at the same time. An employee, as opposed to a contractor, is ordinarily not allowed to carry on a private business. In this connection, it is the power to engage in other activities, not the actual extent to which it is done, which is important; an independent contractor may well devote full time to the job. While respondent's other activities were not very extensive, they seem clearly to negative the status of an employee. He continued in his capacity as inactive president of the bank at Ocala, and continued to attend directors' meetings (R. 50). This would, even apart from statutory provision, be a matter of very doubtful propriety were respondent in fact an employee of the State department which supervised banks. But when the Florida statutes are considered, it seems fairly clear that respondent could not have continued as director and inactive president of the Ocala bank and at the same time have been an employee of the Comptroller. The Comptroller's banking supervision is accomplished through assistants, of whom only the bank report analyst and the bank examiners are provided for by statute. None of these can be appointed if he has connections with a bank (Rev. Gen. Stats., Sec. 4159, as amended, *infra*). If respondent were in fact an employee of the Comptroller, it is unlikely that he should be allowed to maintain his banking

connections, much less that he should be subject to the same examination by bank examiners as are active institutions.

Finally, there is the question of the extent of the control which the Comptroller exercised over respondent. An absence of control by the State officials was given decisive weight in *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 520–521:

> Nor do the facts stated in the bill of exceptions establish that the plaintiffs were "employees" within the meaning of the statute. So far as appears, they were in the position of independent contractors. The record does not reveal to what extent, if at all, their services were subject to the direction or control of the public boards or officers engaging them. In each instance the performance of their contract involved the use of judgment and discretion on their part and they were required to use their best professional skill to bring about the desired result. This permitted to them liberty of action which excludes the idea of that control or right of control by the employer which characterizes the relation of employer and employee and differentiates the employee or servant from the independent contractor. * * *

The petition alleged that respondent "was continuously under the direction and control of the Comptroller" (R. 7). The answer denied this (R. 48). The Board, after hearing the evidence

(R. 1), found that, while respondent was "under the direct supervision of the Comptroller", his only relation to the State was "that of contract, under which there is an obligation to furnish service, for practical purposes not unlike a contract to sell and deliver a commodity" (R. 50, 52). It must therefore be taken as conclusive (see *supra*, p. 37) that the control which the Comptroller in fact exercised over respondent was of a character such that the relationship was one of contract rather than of employment.

Such facts as the record discloses tend to indicate that this was the case. The respondent supervised a number of persons employed in various capacities in liquidating the insolvent institutions the affairs of which he was conducting (R. 50). Respondent had been the president of a bank and was inactive president of the Ocala bank during the years in question (R. 50). His qualifications show him to be a man of judgment, discretion and professional skill. It is most unlikely that the Comptroller's supervision (Section 4162, Rev. Gen. Stats., *infra*) extended beyond directing respondent *what* to do—i. e., liquidate the institutions—or that the Comptroller directed respondent *how* to do this. In any event, the record does not show to what extent, if any, the respondent's services were in fact subject to the direction and control of the Comptroller, nor does it show that the performance of his duties as liquidator did not involve the use

of his judgment and discretion, requiring the respondent's best professional skill and a full liberty of action. In view of the findings of the Board, it must be taken that the evidence showed the exercise of the independent judgment and liberty of action which distinguishes the contractor from the employee.

To render one an employee, the right of control must be complete and extend to the details of the work. *Childers* v. *Commissioner,* 80 F. (2d) 27 (C. C. A. 9th); *Commissioner* v. *Modjeski,* 75 F. (2d) 468, 471 (C. C. A. 2d), certiorari denied, 295 U. S. 764. The test for determining whether one is an employee or an independent contractor was well formulated in *Haight* v. *Commissioner,* 52 F. (2d) 779, certiorari denied, *sub nom. Adcock* v. *Commissioner,* 285 U. S. 537, where the Circuit Court of Appeals for the Seventh Circuit said (p. 781):

> The record in this case shows that Adcock, in rendering his services to the sanitary district, was under the general direction and supervision of its general attorney. This was required by the rules and regulations of the board of trustees. All this amounts to is that Adcock would report to the general attorney from time to time as to what had been done, and consulted with him. It does not show that the general attorney exercised any detailed control as to what should be done, and how it should be done, which is essential to the relationship of employer and employee.

We submit that the same considerations which have required the conclusion that a lawyer, carrying on his general practice, who is engaged by a state and its political subdivisions and public agencies is not an officer or employee of the state or subdivision or agency (*Lucas* v. *Reed,* 281 U. S. 699; *Lucas* v. *Howard,* 280 U. S. 526; *Buckner* v. *Commissioner,* 77 F. (2d) 297 (C. C. A. 2d) apply with equal force to a bank president who is engaged to render the equivalent of professional services as a liquidator of banking institutions.

In result, the statutes of Florida, the method of appointment and compensation, the continued service as inactive president and director of a bank, and the freedom from control by the Comptroller, all indicate that respondent was not an employee but in substance an independent contractor undertaking to liquidate specified insolvent banks and trust companies. He is, therefore, subject to federal taxation upon the net income realized in this activity.

CONCLUSION

The tax in question is not forbidden by the implications of the Constitution, in that it is imposed (1) with respect to an activity which is not an essential governmental function, (2) on compensation derived from private rather than State funds, and (3) on the compensation of one who is neither an officer nor an employee of the State.

Any one of these propositions is sufficient to support the determination of the Commissioner and the decision of the Board of Tax Appeals. The judgment of the court below should, therefore, be reversed.

Respectfully submitted.

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NOVEMBER 1937.

APPENDIX A

Revenue Act of 1928, c. 852, 45 Stat. 791:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits, and income derived from any source whatever.
>
> * * * * * *

Revenue Act of 1932, c. 209, 47 Stat. 169:

Section 22 (a), in so far as here pertinent is substantially the same as Section 22 (a) above quoted.

Florida Laws of 1929, vol. 1, c. 13576:

> SECTION 14. That Section 4159 of the Revised General Statutes be amended so as to read as follows:
>
> "SECTION 4159. That the Comptroller in the supervision of banks and trust companies, shall have power to employ a bank report analyst and not more than twelve discreet and competent persons to examine into the affairs of every bank, banker, banking company or trust company doing business in the State, and liquidators thereof, except National Banks, and the persons so em-

ployed shall have power to make a thorough examination into all the affairs of each and every such bank, banker, banking firm, banking company or trust company and liquidating agencies, at any time; and in doing so shall have access to all the books, papers, records, securities and assets of all kinds, and shall be authorized to examine any of the officers, directors, agents or employees, of such bank, banker, banking firm, banking company, trust company or liquidators thereof, under oath, and such examiners shall make a full and detailed report to the Comptroller of the conditions of each bank, banking company, trust company or liquidating agency thereof so examined. Provided, that no person connected with the banking business, either as an officer, director, agent or employee shall be so employed."

SECTION 16. That Section 4161 of the Revised General Statutes of the State of Florida be amended so as to read as follows:

"SECTION 4161. EXAMINATION OF BANKS AND TRUST COMPANIES, EXAMINATION FEES. That each bank, banking firm, banking company, trust company and liquidating agency, doing business in the State of Florida, except National Banks, shall be examined at least twice in each year, and oftener if deemed necessary; and for each examination so made each bank, banker, banking firm, banking company, or trust company shall pay into the State Treasury an examination fee based upon the resources of each bank or trust company as follows: * * *"

SECTION 19. That Section 4162 of the Revised General Statutes of the State of Florida be amended so as to read as follows:

"SECTION 4162. COMPTROLLER MAY APPOINT LIQUIDATOR; DUTIES OF LIQUIDATOR; NOTICE TO BANK OFFICERS; CONFIRMING APPOINTMENT. On becoming satisfied, from the reports furnished to him by a State Bank Examiner, or upon other satisfactory evidence thereof, that any bank, banking firm, banker, banking or trust company, or corporation doing business in this State under the State laws, has become insolvent and is in default, or that the affairs of any bank, banker, banking firm or trust company or corporation doing business in this State, under such State laws, is in an unsound condition, or threatened with insolvency because of illegal or unsafe investments, or that its liabilities exceed its assets, or that it is transacting business without authority of law or in violation of law, or if the directors of any bank, banking or trust company, or corporation, or any banker or the management of any banking firm doing business in this State under the State laws, shall knowingly violate, or knowingly permit any of its officers, agents or servants to violate any of the provisions of law relative to such bank, bankers, banking firms, banking or trust companies, or corporations doing business in this State, the rights, privileges and franchises shall be subject to be forfeited, and the State Comptroller may in his discretion forthwith designate and appoint a liquidator to take charge of the assets and affairs of such bank, and require of him such bond and security as the Comptroller deems proper, not exceeding double the amount that may come into his hands, and such liquidator shall be subject to dismissal by the Comptroller, whenever in his judgment such dismissal is deemed neces-

sary or advisable; when one liquidator is dismissed, another may be duly designated and appointed. Such liquidator under the direction and supervision of the Comptroller, shall take possession of the books, records and assets of every description of such bank, banker, banking firm, banking and trust company, or corporation, and in his name shall sue for and collect all debts, dues and claims belonging to it, and upon the order of a court of competent jurisdiction may sell or compound all bad or doubtful debts, and, on a like order, may sell all the real and personal property of such bank, banker, banking firm, banking and trust company, or corporation, on such terms as the court shall direct; and may, if necessary, to pay the debts of such bank, banker, banking firm, banking and trust company, or corporation, sue for and enforce the individual liability of the stockholders. Such liquidator shall pay all money received by him to the State Treasurer to be held as a special deposit for the use and benefit of the creditors, subject to the order of the Comptroller, and shall also make quarterly reports to or when called upon, to the Comptroller of all of his acts and proceedings. The Comptroller, immediately upon appointing such liquidator, shall serve notice upon the president, or upon any vice-president or cashier, or upon any director or other person having the charge or management of any such bank, banker, banking firm, banking or trust company, or corporation, informing him or them in such notice of his action in appointing such liquidator, and notifying him or them or it that he would apply on a date therein named, not to exceed ten days from the date of service of such notice, to some circuit judge

having jurisdiction over the same, for an order confirming his action and the appointment of a liquidator for such banking institution and such bank, banking firm, or banking or trust company, or corporation may, at such hearing contest before such circuit judge the rightfulness and legality of such action of the Comptroller in appointing such liquidator."

SECTION 20. The Comptroller may provide for the administration of the affairs of institutions under the above section by one general liquidator who shall be designated by the Comptroller as a General Liquidator for the administration of the affairs of several or all of the instructions in liquidation, whose compensation shall be paid by the Comptroller, to be paid in such proportions out of the assets of the institution whose affairs are being administered as the Comptroller may determine, not exceeding in the aggregate Six Thousand ($6,000.00) Dollars per annum. The Comptroller may provide for the transfer at any time to the general liquidator of the affairs of any institution for which a particular liquidator or receiver has been heretofore or shall hereafter be designated and the general liquidator shall be thereupon vested with all the rights conferred by law on such general liquidator as if he had been designated in the first instant to act as such.

SECTION 21. That Section 4164 of the Revised General Statutes of the State of Florida be amended so as to read as follows:

"SECTION 4164. EXPENSES OF LIQUIDATING AGENT OR AGENTS; COMPENSATION OF LIQUIDATORS; DEPOSITION OF BANK'S FUNDS.—All expenses of any liquidator shall be paid out of the assets of such bank, banker, banking firm, banking or trust company, or corpora-

tion before distribution of the proceeds thereof. The compensation of the liquidator shall be fixed by the Comptroller, and shall be based upon the amount of work actually necessary and performed, and shall in no case exceed five per cent of the cash collections. From time to time, after full provisions having first been made for the expenses of the liquidating agency, and the payment of liens for taxes and preferred claims, the Comptroller shall make ratable dividend of the money in the hands of the State Treasurer on all such claims as may have been proved to his satisfaction or adjudicated in a court of competent jurisdiction, and as the proceeds of the assets of such bank, banker, banking firm, banking or trust company, or corporation, are paid over to the liquidator, shall make further dividends on all claims previously proved or adjudicated; and the remainder of the proceeds, if any, after all claims have been paid, shall be paid over to the shareholders, of such bank, banker, banking firm, banking or trust company, or corporation, or their legal representatives in proportion to the stock by them respectively held, or their interest therein as appearing."

SECTION 22. That Section 4165 of the Revised General Statutes of the State of Florida be amended so as to read as follows:

"SECTION 4165. COMPTROLLER MAY PURCHASE PROPERTY TO PROTECT LIQUIDATOR'S TRUST.—Whenever any liquidator, duly appointed by the Comptroller, and who shall have qualified and entered upon the discharge of his trust, shall find it in his opinion necessary to fully protect and benefit his said trust, to the extent that said trust may have in any property, real or personal, by reason of any bond, mortgage, lien, assign-

ment, equity or other proper legal claim attaching thereto, and which said property is to be sold under execution, decree or foreclosure, or any proper order of any court of competent jurisdiction, or reclaimed or repossessed by any person having title opposed to such equity of his trust, he may certify the facts in the case, together with his opinion as to the value of the property, and the value of the equity his trust may have in same, and the amount that may be necessary to purchase such property, to the Comptroller, and if the Comptroller shall in his judgment deem it to the best interest of the said trust, he shall be and is empowered to draw upon the funds to the credit of said trust in the hands of the State Treasurer to the amount necessary for the purchase of said property for the said trust."

Treasury Regulations 74:

ART. 56. STATE CONTRACTS.—The profit of an independent contractor from a contract with a State or political subdivision thereof must be included in gross income. * * *.

ART. 643. COMPENSATION OF STATE OFFICERS AND EMPLOYEES.—Compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function of the State or political subdivision, including fees received by notaries public commissioned by States, is not taxable. Compensation received for services rendered to a State or political subdivision thereof is included in gross income unless (a) the person receives such compensation as an officer or employee of a State or political subdivision, and (b) the services are rendered in connection with the exercise of an essential governmental function. The commissions of receivers appointed by State

courts are subject to tax for 1928 and subsequent taxable years.

An officer is a person who occupies a position in the service of the State or political subdivision, the tenure of which is continuous and not temporary and the duties of which are established by law or regulations and not by agreement. An employee is one whose duties consist in the rendition of prescribed services and not the accomplishment of specific objects, and whose services are continuous, not occasional or temporary. * * *

Treasury Regulations 77:

Article 56 and Article 643 are identical with the corresponding articles of Treasury Regulations 74, quoted above.

APPENDIX B

There follows a very rough classification of the procedures adopted by the several States for the liquidation of insolvent banking institutions:

1. Administrative determination of insolvency, followed by judicial confirmation and appointment of receiver subject to full judicial supervision: South Carolina, Code of 1932, Sections 7852–7855; Virginia, Code of 1936, sec. 4149 (52).

2. Administrative determination of insolvency, followed by mandatory appointment of state banking official as receiver, subject to full judicial supervision: Connecticut, General Statutes (1935 Supp.), Secs. 1437c; Delaware, Revised Code, 1935, Secs. 2294–2297; Iowa, Code of 1935, Secs. 9239–9243; Maine, Revised Statutes, 1930, ch. 57, Sec. 52; Michigan, Annotated Statutes, 1937, Sec. 2364 (as amended by Financial Institutions Act, 1937); Minnesota, Statutes, 1927, sec. 7682, and Laws of 1933, ch. 232; New Hampshire, Public Laws, 1926, ch. 268; New Mexico, Laws of 1933, ch. 32; North Dakota, Laws of 1931, ch. 96, Secs. 50–51; Rhode Island, General Laws, 1923, ch. 274, Sec. 7; South Dakota, Compiled Laws, 1929, Secs. 8924–8937; Tennessee, Code of 1932, Secs. 5964–6000; Texas, Vernon's Statutes, Banks, Articles 368–371, 451–474; Vermont, Public Laws of 1933, Secs. 6749–6760.

3. Administrative determination of insolvency, followed by administrative liquidation or administrative appointment of receiver; subject to limited judicial supervision: Arizona, Revised Code (1928 and 1936 Supp.), Secs. 245–249; Arkansas,

Pope's Digest, Secs. 738–739, 767–770; California, General Laws, Act No. 652; Colorado, Compiled Laws, 1921, Secs. 2725–2750; Florida, Revised General Statutes 4162–4167; Illinois, Jones' Statutes, Sec. 10.11; Kansas, General Statutes, Sec. 9–130; Kentucky, Carroll's Statutes, 1936, Secs. 165a–16, 165a–17; Louisiana, General Statutes, 1932, Secs. 697–715; Maryland, Annotated Code (1924 and 1935 Supp.), Art. 11, Secs. 8–9D; Massachusetts, General Laws, 1932, ch. 167, Secs. 22–36; Mississippi, Code of 1930, Secs. 3816–3817; Missouri, Revised Statutes, 1929, Secs. 5316–5323; Montana, Revised Code, 1935, Secs. 6014.131–6014.150; Nebraska, Compiled Statutes, 1929, Secs. 8–184, 8–194; New Jersey, Compiled Statutes, pp. 173–178, Cumulative Supplement 1911–1924, Secs. 17–24; New York, Banking Law, Secs. 57–81; North Carolina, Code of 1935, ch. 5, Sec. 218; Oregon, Code, Secs. 22–1901 to 22–2019; Pennsylvania, Purdon's Statutes, Title 7, Secs. 21–50; Utah, Revised Statutes, 1933, ch. 7–2; West Virginia, Code of 1931 (as amended in 1937), ch. 31, Sec. 32; Wisconsin, Statutes, 1935, Sec. 220.08; Wyoming, Revised Statutes, 1931, Secs. 10–501 to 10–528.

4. Administrative determination of insolvency, followed by administrative liquidation or receivership, subject to judicial review only on objection of claimants, etc.: Alabama, Civil Code of 1923, Secs. 6299–6324; Georgia, Code of 1937, Secs. 13–801, *et seq.;* Idaho, Code of 1932, Secs. 25–901, *et seq.;* Nevada, Compiled Laws, 1929, Secs. 702–711; Ohio, General Code, 1936, Secs. 710–88a to 710–106; Oklahoma, Laws of 1937, ch. 40, Secs. 72–87; Washington, Remington's Revised Statutes, Secs. 3266–3280.

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